1956

Andrew G. Nokes v. Continental Mining & Milling Co. et al : Brief of Appellants

Utah Supreme Court

Gustin, Richards, Mattson & Evans; Attorneys for Defendants and Appellants;

Case No. 8501

IN THE SUPREME COURT
of the
STATE OF UTAH

ANDREW G. NOKES,

Plaintiff and Respondent,

—vs.—

CONTINENTAL MINING & MILLING CO., a Corporation, E. G. FRAWLEY, President, JOHN DOE, Secretary, GLEN I. CRANDALL, Transfer Agent,

Defendants and Appellants.

BRIEF OF APPELLANTS

Appeal from the District Court of the Third Judicial District in and for the County of Salt Lake
HONORABLE DAVID T. LEWIS, *Judge*

GUSTIN, RICHARDS, MATTSSON & EVANS
Attorneys for Defendants and Appellants

INDEX

TABLE OF CASES

STATUTES

TEXTS

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STATEMENT OF THE FACTS

This is an action to compel the defendant corporation, its officers or Transfer Agent to transfer a certificate of stock on the books of the corporation. The certificate in question represented 100,000 shares of the common stock of the defendant Continental Mining and Milling Company, a Nevada corporation. The certificate was made in the names of Lawrence & Mario O. Migliac-

cio (Plaintiff's Ex. 1, R. 29), and, being promotion stock, was deposited in 1950 with the Utah Securities Commission. The stock was released at the request of the plaintiff and over the objection of the defendant corporation by the Utah Commission on the 7th day of June, 1954 (R. 51). The transfer of the stock was arranged for the specific purpose of defeating the corporation's rights and under such circumstances that dispel any notion of a transfer in good faith. The defendant corporation and defendant E. G. Frawley take this appeal.

The sale of the stock was arranged by Thomas C. Cuthbert and John W. Lowe, attorneys licensed to practice before the Bar of this State (R. 46, 51). They were and now are the attorneys for the Migliaccios and had previously represented them in prolonged litigation against the defendant corporation and the defendant Frawley (R. 49). Cuthbert and Lowe were also close personal friends of the plaintiff to the extent that all considered a relationship of trust and confidence existed among them (R. 44, 51).

On the 7th of June, the date the Utah Commission released the certificate to the Migliaccios, Cuthbert and Lowe were present and represented Migliaccio, and had personal knowledge of the corporation's claim and all of the circumstances surrounding the disputed stock and were advised that the corporation intended to institute an action to recover the certificate (R. 46, 51, 53). On the 11th day of June, four days later and five days prior to the sale to the plaintiff, the defendant corporation

filed a complaint in the United States District Court for the District of Utah, Central Division, wherein it claimed to be the owner of said stock (Ex. 3, R. 42). Mr. Lowe knew that the action had been commenced (R. 53).

The sale of the stock was arranged on the 16th day of June, 1954, by a series of coincidences. On that day the plaintiff, a resident of Kansas, as good fortune would have it, was in the offices of Cuthbert and Lowe, apparently upon business for his former employer, Pioneer Pipe Line Company, which company Cuthbert and Lowe represented (R. 34-35). Mr. Nokes had gone to law school with Cuthbert where their friendship began, and on the 16th day of June, 1954, Mr. Nokes was an attorney licensed to practice in the State of Utah (R. 36, 44). He was employed, however, at that time by the Sinclair Pipe Line Company for a salary of about $500.00 per month (R. 42). Cuthbert knew Nokes was a novice and lacking in any knowledge about uranium stock (R. 45), except that he had heard there was money to be made in uranium stock (R. 35).

While the record discloses that Nokes was in the office on matters relating to litigation involving the Pioneer Pipe Line Company, it does not appear that any business was discussed except the sale of the stock. The suggestion that Nokes buy the stock and the price at which it could be purchased was made by Cuthbert and Lowe (R. 35-37). The benefits and the speculative possibilities of the stock were discussed in detail (R. 38-45). As coincidence would have it Nokes was receptive to a

speculation and had $500.00 with which to indulge his mood (R. 35). Notwithstanding the fact that the stock was not traded, had no market value and required Nokes to part with an entire month's salary, there was absolutely no sales resistance (R. 38-45). The conversations were held in Mr. Lowe's office while all three were present and their very good friend and fellow member at the Bar was induced to purchase the stock upon the representation that it had a book value of $7000.00 (R. 45).

In view of the extemporaneous nature of the conversations about stock a further remarkable coincidence was at hand. The Migliaccios were residents of Price and, in spite of the fact that it took a United States Marshal from the 11th day of June until the 19th day of July to discover the whereabouts of Mr. and Mrs. Migliaccio, Mr. Cuthbert, by means of a single telephone call, located Migliaccio in the Atlas Building in Salt Lake City (R. 38-48). At this point favorable circumstances continued. Rather than call his client from Lowe's office by merely reaching out and picking up the telephone, Mr. Cuthbert left Mr. Lowe's office and, in the seclusion of his own office, had the following conversation with Migliaccio:

> " 'So I called Magliaccio on the telephone thereafter and told him that if he wanted money I could get him $500.00 for this stock.
>
> Magliaccio said: 'Do you think it is a good deal?'
>
> I told him we knew he had been fighting it out with Frawley since about 1950, that it was a

> sure bet he wouldn't be able to do anything with that stock without litigation. If he sold the stock off maybe somebody else could do something with it without fighting it. So I told him on that basis it would be a good deal to get out of it because lawsuits would be costing more than the stock was worth.' " (R. 48).

Upon completing the conversation with Migliaccio Cuthbert returned to Mr. Lowe's office (R. 48). Good fortune continued on behalf of their very good friend Mr. Nokes because he was informed by Mr. Cuthbert that the sale had been arranged. Another remarkable circumstance then occurred. Mr. Cuthbert forgot to tell his very good friend all of the conversation he had with Migliaccio (R. 48).

In about an hour's time all of these matters occurred and Nokes hurried to meet Migliaccio, turn over to him a month's salary, before deductions, and went to an office of the defendant Frawley to demand transfer (R. 39). At this point the course of things changed. From the facts it can hardly be said that the change was unexpected. On seeing Mr. Frawley, Nokes' good fortune began to frown because, as he testified: "After he belabored me with invective he told me he would not transfer the shares." (R. 40). Nokes then hurried back to the office of Cuthbert and Lowe and told them of the turn of events (R. 39). Thus, two hours after they had made their good friend $7000.00 on a $500.00 investment, on stock that was not traded and was not worth the price of a lawsuit, Cuthbert and Lowe told Nokes that the defendant corporation claimed the stock (R. 41-48).

Fortune continued to frown on Mr. Nokes because his request that his friends represent him in the matter was refused (R. 50).

The defendant corporation thereafter continued to assert its rights and following the trial of the action filed in the Federal Court, Judge A. Sherman Christenson, on the 14th day of April, 1955, adjudicated that the corporation was the owner of the stock. (Ex. 4, R. 42).

The record discloses that the only demand for transfer made was on Mr. Frawley. It does not show that the demand was made in the office of the Continental Mining and Milling Company or that the stock was sent to the Transfer Agent of the corporation for transfer (R. 31).

The defendants contend that the plaintiff acquired nothing by the endorsement and, in any event, the plaintiff had notice of the defect and claim of the defendant corporation and that the sale was not made in good faith.

STATEMENT OF POINTS

POINT I.

PLAINTIFF IS BOUND BY THE ADJUDICATION THAT THE CORPORATION WAS THE OWNER AND DEFENDANTS' PREDECESSORS HAD NO RIGHT, TITLE OR INTEREST IN THE STOCK.

POINT II.

PLAINTIFF HAD ACTUAL KNOWLEDGE OF THE DEFECT IN TITLE OF THE STOCK OR THAT THE SALE WAS MADE UNDER CIRCUMSTANCES WHICH IMPUTE NOTICE OF THE DEFECT.

POINT III.

THE SALE WAS NOT MADE IN GOOD FAITH.

POINT IV.

THAT BY STATUTE THE TRANSFER WAS NOT VALID AS AGAINST THE CORPORATION UNTIL IT WAS REGISTERED UPON THE BOOKS OF THE CORPORATION.

ARGUMENT

POINT I.

PLAINTIFF IS BOUND BY THE ADJUDICATION THAT THE CORPORATION WAS THE OWNER AND DEFENDANTS' PREDECESSORS HAD NO RIGHT, TITLE OR INTEREST IN THE STOCK.

The position of the defendant is that the plaintiff is bound by the decree in Continental Mining and Milling Company, a corporation, plaintiff, v. Lawrence and Marie O. Migliaccio, defendants, Civil C-85-54, United States District Court for the District of Utah, Central Division. In the case referred to the specific question before the court was the title and ownership of the certificate and the stock it represented. The same matter is directly in question in the present action. In such cases it has been held that the judgment of a court of concurrent jurisdiction is conclusive as between the parties and those in privity with them in estate or law. *Matthews v. Matthews et al.,* 102 Utah 428, 132 P. 2d 111:

> " 'The judgment of a court of concurrent jurisdiction, directly upon the point, is as a plea, a bar, or as evidence, conclusive, between the same

parties, upon the same matter directly in question in another court.' 15 R.C.L. 951, Sec. 429.

'The foundation principle upon which the doctrine of res judicata rests is that parties ought not to be permitted to litigate the same issue more than once; that, when a right or fact has been judicially tried and determined by a court of competent jurisdiction, or an opportunity for such trial has been given, the judgment of the court, so long as it remains unreversed, should be conclusive upon the parties, *and those in privity with them in law or estate.*

* * * Public policy and the interest of litigants alike require there be an end to litigation, and the peace and order of society demand that matters distinctly put in issue and determined by a court of competent jurisdiction as to parties and subject matter shall not be retried between the same parties in any subsequent suit in any court.' 15 R.C.L. 953, Sec. 430." (Emphasis added).

While the plaintiff was named a party to the action after the defendant became aware of the transfer, he was never served with process. However, the plaintiff is in privity with the defendants therein, having succeeded to the same property and property rights. This court defined the word "privity" in relation to the doctrine of res judicata in *Tanner v.* ***Bacon, State Engineer,*** *et al.,* 103 Utah 494, 136 P. 2d 957:

"It is well settled that the doctrine of res judicata does not operate to affect strangers to a judgment; that it only affects the parties and their successors in interest, and those who are in privity with a party thereto. 30 Am. Jur. 951,

> Sec. 220; 34 C. J. 756 to 758, Section 1165; Glen Allen Mining Co. v. Park Galena Mining Co., 77 Utah 362, at 367, 296 P. 231; State Bank of Sevier County v. American Cement & Plaster Co., 80 Utah 250, 10 P. 2d 1065; Tintic Indian Chief Mining & Milling Co. v. Clyde, 79 Utah 337, 10 P. 2d 932; Taylor v. Barker, 70 Utah 534, 262 P. 266, 55 A.L.R. 1032; Mill v. Brown, 31 Utah 473, 88 P. 609; 120 Am. St. Rep. 935. This court has defined the word 'privity' as 'a mutual or successive relationship to the same right or property. As applied to judgments or decrees of courts, the word means one whose interest has been legally represented at the time.' Glen Allen Mining Co. v. Park Galena Mining Company, supra (77 Utah 362, 296 P. 233)."

The plaintiff herein could acquire only the title of his predecessors in interest and nothing more. The question of title was fully litigated and the plaintiff herein could offer no matter in support of his transferor's title nor impose any defense thereto. His interest was legally represented in the fullest sense of the word. The essential and important element of privity is that one person should succeed to the estate or interest formerly held by another. The definition of privity and the theory are set forth in 1 *Freeman on Judgments,* Fifth Edition, Section 438, pages 959-961, as follows:

> "Privies in General. — 'Where one claims in privity with another, whether by blood, estate, or law, he is in the same situation with such person as to any judgment for or against him; for judgments bind privies as well as parties.' The rule is well settled and elementary that a judgment is as conclusive on privies as on the parties them-

selves. 'The term ''privity'' denotes mutual or successive relationship to the same rights of property.' This relationship is produced either by operation of law, by descent, or by voluntary or involuntary transfers from one person to another. Hence privies have, from an early period in the history of the common law, been classified as, —

* * *

All privies are in effect, if not in name, privies in estate. They are bound because they have succeeded to some estate or interest which was bound in the hands of its former owner; and the extent of the estoppel, so far as the privy is concerned, is limited to controversies affecting this estate or interest. The manner in which the estate was lawfully acquired neither limits nor extends the operation of the estoppel created by a former adjudication, and is therefore immaterial. It is essential to privity, as the term is here used, that one person should have succeeded to an estate or interest formerly held by another."

In the case herein the complaint in the United States District Court was filed on the 11th day of June, 1954, and the transfer of the stock was on the 16th day of June, 1954, the defendant Migliaccio, however, was not served until July 19, 1954. In discussing privity the sequence in which the acts occurred are of importance. It has been held that where the transfer is prior to the commencement of the action there is no privity, but where the transfer is made subsequent to the commencement of the action there is privity and the party is bound by the judgment. The question as to when the action was commenced is also important. The Utah Rules of Civil Pro-

cedure provide that an action may be commenced by the filing of a complaint or by the service of summons. *Utah Rules of Civil Procedure,* Rule 3 (a). The Federal rules provide that an action is commenced by filing a complaint with the court. *Federal Rules of Civil Procedure,* Rule 3. The Federal Court action was necessarily commenced by the filing of the complaint and it is that date which is critical in determining the question of privity and not the service of process or the date of adjudication. It is interesting to note the comment in 1 *Federal Practice and Procedure,* Barron and Holtzoff, Section 161 at page 270:

> "The necessity and importance of the rule is obvious. The time of commencing the action determines whether it is prematurely brought or whether by reason of delay it is barred by limitations or laches, or which of two courts first acquired jurisdiction and therefore should retain the case for disposition, *or in some cases whether after-accruing claims and defenses may be litigated.*" (Emphasis added).

The same proposition is stated in 1*Freeman on Judgments,* Fifth Edition, Section 440 at page 966:

> "Judgment Against Predecessor After Transfer. — It is well understood, however, though not always so stated in express terms, that no one is privy to a judgment whose succession to the rights of property thereby affected, occurred previously to the institution of the suit. No alienee, grantee, assignee or mortgagee is bound or affected by a judgment or decree in a suit commenced by or against the alienor, grantor, assignor or mortgagor, subsequent to the alienation, grant, assign-

ment or mortgage, to which he was not a party.

> The critical date in determining the question of a purchaser's privity is the commencement of the suit rather than the date of the adjudication, except that this may be affected by statutes governing lis pendens."

The question is necessarily raised as to what effect the Uniform Stock Transfer Act has on the question here involved. The Uniform Stock Transfer Act was not designed to give a party any greater property rights than before the passage of the Act. It is merely a procedural rule affecting the transfer of stock and is principally effective between the parties. While the purpose is to give the stock some of the incidents of negotiability, it does not go so far as to change a stockholder's relationship with the corporation. The extent of negotiability and the effect of the Uniform Stock Transfer Act was before the court in *Untermyer et al. v. State Tax Commission et al.*, 102 Utah 214, 129 P. 2d 881:

> "Counsel argue that since the Uniform Stock Transfer Act permits attachment or levy of execution on stock only by seizure of the certificate, the stock or interest of the stockholder in the corporation does not exist independent of the certificate. Therefore it can have no situs except the situs of the certificate. *The certificate thus actually becomes the property, and not the evidence or proof of ownership thereof. Such is not the import of the Uniform Stock Transfer Act. It does not change the nature of stock ownership or stockholders' rights, as far as the state or the corporation is concerned. That Act relates solely to methods of transferring title to stock either by*

> *act of the owner, or by legal process.* * * * It is simply a procedural statute dealing with the methods and processes of determining or obtaining title to the stock." (Emphasis added).

The plaintiff, notwithstanding the Uniform Stock Transfer Act, could acquire no greater right nor any better title than his transferor. While the trial court found that the plaintiff had no knowledge of any infirmity or of any court action involving the action, it did not specifically find that the plaintiff herein was not in privity with the defendant in the Federal Court suit. The question of notice is immaterial if, as defendants contend herein, the plaintiff was bound as a privy by the prior judgment.

POINT II.

PLAINTIFF HAD ACTUAL KNOWLEDGE OF THE DEFECT IN TITLE OF THE STOCK OR THAT THE SALE WAS MADE UNDER CIRCUMSTANCES WHICH IMPUTE NOTICE OF THE DEFECT.

While defendants realize that they are faced with an adverse finding of fact by the trial court on the question of notice, they take the position that the testimony of the plaintiff and the witnesses Cuthbert and Lowe are not worthy of belief. From the decisions heretofore handed down by this Court it would appear that whether or not it is to be bound by a finding of fact depends upon the circumstances of each case, contrary to the oft-stated rule that a finding will not be disturbed if there is any evidence to support it.

The factual premise and the circumstances surrounding the sale made it impossible to prove actual notice. Cuthbert and Lowe had knowledge of all of the facts relating to the stock certificate and were legal counsel for Migliaccios and the good friend of the plaintiff Nokes. It was testified that they did not inform Nokes of any defect in relation to the stock prior to the transfer, but within two hours thereafter informed plaintiff of the dispute relating to the stock. It seems indisputable that Cuthbert and Lowe were acting as the agent of both parties, giving their friend an opportunity to buy valuable stock and making it possible for their client to get rid of what ultimately proved to be an adverse lawsuit. If knowledge of defects were not imputed to the plaintiff under the fact situation, it is inconceivable what manner of situation must be created to impute knowledge. The rule is stated in American Jurisprudence as follows:

> "Notice given to an agent employed to purchase property, of any defect in the title to, or quality of the property, is notice to his principal, in any controversy between him and the vendor in relation to such property. Accordingly, it is everywhere conceded that a purchaser is bound and affected by the knowledge or notice of an agent purchasing the property of prior liens, trusts, or frauds, which knowledge or notice the agent obtains in negotiating the particular transaction. The general rule is also applied as to notice, acquired by the agent, of one who claims to be a bona fide purchaser." 2 *Am. Jur.*, Section 371, page 291.

POINT III.

THE SALE WAS NOT MADE IN GOOD FAITH.

In spite of the difficulty relating to proof of actual notice, it is the contention of the defendant that the plaintiff was not a purchaser in good faith. The court made the finding that there were no facts adduced that, by reasonable diligence, plaintiff should have known of any adverse claim. The promise of fantastic profits in uranium stock, not traded, should have been a warning to any purchaser. In this case the plaintiff testified that he knew that the stock was not traded on the market and, in spite of the representation that he could purchase for $500.00 stock having a book value of over $7000.00, the court found that there was no circumstance that would put plaintiff on notice of a defect.

Good faith has been the subject of many definitions but it universally encompasses an honest intent, an absence of malice or design to defraud or seek unconscionable advantage. It has also been said that to constitute good faith there must not only be an absence, not alone of participation in the fraud or collusion with the vendor, but also of knowledge or even notice of the fraud or of facts and circumstances calculated to put an ordinarily prudent business man on inquiry so that he would ascertain the truth.

> "To constitute 'good faith', there must not only be an absence, not alone of participation in the fraud or collusion with the vendee, but also of knowledge or even notice of the fraud, or of facts and circumstances calculated to put an ordinarily

> prudent businessman on inquiry, so that he would ascertain the truth. Thus, where it appeared that a purchaser of stock had suspicions relating to the sale of it, he cannot be said to be a purchaser in good faith. Siano v. Helvering, D. C. N. J., 13 F. Supp. 776, 780." *Words and Phrases,* Vol. 18, page 495.

From the record it would appear that the plaintiff was an ordinarily prudent business man. His employment would indicate at least that, and, while being a lawyer might negative the idea of business judgment, it does not appear in the record that he claimed any such infirmity.

While the defendant herein is faced with the finding as to notice, it is more fortunate on the question of good faith. No finding was made to the effect that the plaintiff was a purchaser in good faith. It would seem strange, under the circumstances, that the plaintiff should not be charged with at least making the nominal effort of a local telephone call to inquire about the stock. If the conduct of plaintiff was not for the purpose of colluding to gain an unconscionable advantage, why such a calculated effort to talk about everything except the wrong things. Why was it necessary for Cuthbert to adjourn to another office to call Migliaccio and why didn't he inform plaintiff of the conversation. In response to the question why he didn't tell Nokes about the conversation with Migliaccio, Cuthbert answered: "I didn't believe there was anything wrong with the stock." (R. 49).

Because Cuthbert did not tell Nokes about his conversation with Migliaccio for the reason that he didn't

believe there was anything wrong with the stock, he was asked if his statement to Migliaccio "that it was a sure bet he wouldn't be able to do anything with that stock without litigation" was the truth. He answered that it was. If one is to take the answers as the truth, the only result is a calculated attempt by Cuthbert and Lowe to seek an unconscionable advantage in which the plaintiff must be regarded as a participant.

POINT IV.

THAT BY STATUTE THE TRANSFER WAS NOT VALID AS AGAINST THE CORPORATION UNTIL IT WAS REGISTERED UPON THE BOOKS OF THE CORPORATION.

As has been previously noted above, the Uniform Stock Transfer Act is a procedural device and does not change the nature of the stockholders' ownership or rights so far as the corporation is concerned. *Untermyer et al v. State Tax Commission et al.,* supra.

The defendant takes the position that the transfer from Migliaccio to Nokes did not bind the corporation until such time as the transfer was registered on the books of the corporation. Section 1617, *Nevada Compiled Laws* 1929 as amended, provides:

> "* * * No transfer of stock shall be valid against the corporation until it shall have been registered upon the books of the corporation."

Upon presentation of the stock certificate to the President of the corporation plaintiff was informed of the

corporation's claim. The plaintiff had acquired no rights as against the corporation at the time plaintiff was informed of its claim. The refusal to transfer was the only method by which the corporation could protect its rights and the rights of other stockholders, and upon the refusal to transfer the plaintiff was left with an adequate remedy against his transferor and, by reason of the statute, had no right to compel the corporation to make the transfer. Any other construction would leave the corporation and the stockholders with a right but no remedy to safeguard its interests. The corporation's rights could be defeated by successive transfers. The above statute has been construed by two Nevada cases, *Bercich v. Marye,* 9 Nev. 316, and *Double O Mining Co. v. Simrak,* 132 P. 2d 605. The latter case held:

> "A transfer of stock between individuals, in order to receive recognition by the corporation, must be registered upon its books: however, if not so registered, the transfer is binding upon the parties, and the equitable title, at least, passes. Further, as between individuals, a registration upon the corporate books must be made in order that the transferee may be entitled to exercise voting power. In re Argus Printing Co., 1 N.D. 434, 48 N.W. 347, 12 L.R.A. 781, 26 Am. St. Rep. 639, 647; Merchants National Bank v. Wehrmann, 202 U.S. 295, 26 S. Ct. 613, 50 L. Ed. 1036, 1040; 6 Fletcher, Corp., 6339, Section 3796 and n. 19."

A similar California statute has been construed in *Realty & Rebuilding Co. v. Rea et al.* (Cal.), 224 P. 1020:

> "The general rule is that a transferor is not released from this imposed burden until his trans-

fer is duly registered upon the corporate books. Our Code provides in substance that a transfer is not valid, except as to the parties thereto, until the same is entered upon the books of the corporation so as to show the name of the parties by whom and to whom the transfer was made, the number of the certificate, the number of designation of the shares, and the date of the transfer. Civ. Code, Sec. 324. This statute is mandatory, and not directory, and is not a mere rule for guidance of the corporation and stockholder. The section makes the transfer invalid, except as between the parties thereto, unless it is made in conformity with this statutory requirement. The transfer of shares of stock, therefore to become effectual between transferor and creditors of the corporation, must be entered on the corporate books. Spreckels v. Nevada Bank, 113 Cal. 272, 45 Pac. 329, 33 L.R.A. 459, 54 Am. St. Rep. 348. A provision of this character is a formality intended for the protection and security of the corporation and of third persons dealing with the same. Creditors of a corporation have a right to rely upon the books as showing who the stockholders are and the amount of stock held by each, and failure to make a transfer on the books of the corporation requires that such transfer must be disregarded in considering the rights of creditors. Sherman v. S.K.D. Oil Co., 185 Cal. 534, 548, 197 Pac. 799 and cases cited."

It is also of importance to note that the request for transfer was made to Mr. Frawley. There is no evidence in the record that it was made in the office of the defendant corporation, and the plaintiff testified that he did not present the stock certificate to the Transfer

Agent. The books of the defendant corporation are by law required to be at its principal place of business in Nevada, the only place where the transfer could lawfully be made.

CONCLUSION

It is respectfully submitted that the judgment should be reversed.

GUSTIN, RICHARDS, MATTSSON & EVANS

Attorneys for Defendants and Appellants